

DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 02-0391
Sales and Use Tax
For the Years 1998, 1999, 2000

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ISSUES

I. Sales and Use Tax- Retail Sales

Authority: IC 6-2.5-2-1, IC 6-8.1-5-1, IC 2.5-4-4, IC 6-2.5-5-26 (b), 45 IAC 2.2-5-58, Indiana Bell Telephone Co. v. Indiana Department of Revenue, 627 N.E. 2d 1386, Ind. Tax Court (1994), Raintree Friends Housing v. Indiana Department of Revenue, 667 N.E.2d 810 (Ind. Tax 1996), Black's Law Dictionary 213 (5th ed. 1979).

The taxpayer protests the assessment of sales tax on certain retail sales.

II. Sales and Use Tax-Capital Assets

Authority: IC 6-2.5-3-2 (a), IC 6-2.5-5-25 (a), 45 IAC 2.2-3-8, Sales Tax Division Information Bulletin #10 Revised February 10, 1986.

The taxpayer protests the assessment of use tax on certain capital assets.

III. Sales and Use Tax-Supplies

Authority: IC 6-2.5-3-2 (a), IC 6-2.5-5-25 (a), Sales Tax Division Information Bulletin #10 Revised February 10, 1986.

The taxpayer protests the assessment of use tax on certain supplies.

IV. Tax Administration-Penalty

Authority: IC 6-8.1-10-2.1, 45 IAC 15-11-2.

The taxpayer protests the assessment of the negligence penalty.

STATEMENT OF FACTS

The taxpayer is a not-for-profit corporation that operates a living museum with demonstrations and a recreation of a turn-of-the-century village and farmstead. The corporation also operates a hotel adjacent to, and affiliated with, the living museum. After an audit, the Indiana Department of Revenue, hereinafter referred to as the “department,” assessed additional sales and use tax, interest and penalty. The taxpayer protested the assessment and a hearing was held.

I. Sales and Use Tax- Retail Sales

DISCUSSION

All tax assessments are presumed to be accurate and the taxpayer bears the burden of proving that any assessment is incorrect. IC 6-8.1-5-1 (b). Indiana imposes an excise tax, the sales tax, on retail sales of tangible personal property. IC 6-2.5-2-1 (a). The rental of a hotel room and booths for less than thirty (30) is defined as a retail sale subject to the sales tax. IC 2.5-4-4. Purchasers are liable for the tax that the retail merchants collect and remit to the state. IC 6-2.5-2-1(b). Sales by not-for-profit corporations are exempt from the sales tax if “the property sold is designed and intended primarily either for the organization’s educational, cultural, or religious purposes, . . .” IC 6-2.5-5-26 (b). It is established law that all tax exemptions must be strictly construed against taxpayers. Indiana Bell Telephone Co. v. Indiana Department of Revenue, 627 N.E. 2d 1386, Ind. Tax Court (1994).

Throughout the year, the taxpayer operates a hotel, gift shops, a general store, a refreshment stand and a farmhouse that sells prepared meals. The taxpayer provided the department a trial balance for 1998, 1999, and 2000. Each account was examined and it was determined from this list what accounts sales tax should have been collected on. The accounts included sales tax collected, innkeeper tax collected, exempt sales for which the taxpayer had exemption certificates for room rental at the Inn and the fifteen (15) percent of sales such as jams and jellies that were allowed as exempt from the General Store. Credit was also given for the sales tax remitted. These amounts were deducted from total taxable sales to arrive at additional taxable sales.

The taxpayer protested the sales tax imposed on its hotel room rentals, vending machine sales, consignment sales, penny machine sales, pony feeding machine sales, booth rentals and booth utility fees. The taxpayer argued that these sales were exempt from the imposition of the sales tax pursuant to the exemption granted not-for-profit corporations.

The Indiana Tax Court dealt with the not-for-profit exemptions from income taxes and sales tax in the case Raintree Friends Housing v. Indiana Department of Revenue, 667 N.E.2d 810 (Ind. Tax 1996). In this case, the Court found that a housing corporation that provided retirement housing qualified for the charitable purposes exemptions from the gross income tax, adjusted gross income tax, supplemental net income tax, and sales tax. Since the tax statute does not define the term “charitable,” the Court looked to the definition found in Black’s Law Dictionary 213 (5th ed. 1979) as follows:

Charity is broadly defined as:

A gift for, or institution engaged in, public benevolent purposes. [It is a}n attempt in good faith, spiritually, physically, intellectually, socially and economically to advance and benefit mankind in general, or those in need of advancement and benefit in particular, without regard to their ability to supply that need from other sources and without hope or expectation, if not with positive abnegation, of gain or profit by donor or by instrumentality of charity.

The taxpayer does provide the benevolent service of educating people about a turn of the century Indiana farming village. The education of individuals about the history of Indiana benefits all of society. Further, the taxpayer does not gain personally from the provision of these educational services. The taxpayer's activities meet the definition of charitable as did the retirement center in the Raintree Case. Therefore, the taxpayer's sales that are intended to and do provide this beneficial and educational service qualify for the not-for-profit charitable purpose exemption from the sales tax.

45 IAC 2.2-5-58 discusses the application of sales tax to retail sales made by qualified not-for-profit organizations as follows:

- (a) The state gross retail tax shall not apply to sales by qualified not-for-profit organizations of tangible personal property of a kind designated and intended primarily for the educational, cultural or religious purposes of such qualified not-for-profit organization and not used in carrying out a private or proprietary business.
- (b) The gross receipts from each sale of tangible personal property by a qualified not-for-profit organization are exempt under this rule only if:
 - (1) The nature of the property sold will further the educational, cultural or religious purposes of the organization; and
 - (2) The organization is not carrying on a private or proprietary business with respect to such sales.
- (c) Furthering the educational, cultural or religious purpose. The primary purpose of the property sold must be to further the educational, cultural or religious purpose of the qualified not-for-profit organization.

-EXAMPLE-

- (1) The sale of textbooks and supplies by a parochial, public or private not-for-profit school is exempt if made to students of the school in grades one through twelve. Such sales are primarily intended to further the educational purposes of the school.
- (2) The sale of bibles, choir robes and prayer books by a religious organization is exempt. Such sales are primarily intended to further the religious purposes of the organization.
- (3) The sale of meals by an art gallery is taxable. The meals are intended primarily for the convenience of visitors.

(The sale of textbooks and other educational materials by a secretarial school which is operated for profit is taxable. A profit-making educational enterprise is not a qualified not-for-profit organization under this regulation.

(5) The sale of greeting cards by a church bookstore is taxable. Such sales are not primarily intended to further the religious purposes of the organization.

Not-for-profit status as a charitable corporation does not automatically qualify a corporation for charitable purpose exemption on all sales. Paragraph 2 (c) limits the exemption to those sales that will further the charitable and educational purposes of the not-for-profit corporation.

Feeding the ponies gives visitors the opportunity to engage in an activity appropriate to the time period of taxpayer's facility. This active participation of a visitor in the time specific activity furthers the visitor's knowledge and understanding of a village and farm at the turn of the century. The vending machine sale of pony food is analogous to the exempt sales in example 2. This sale, upon which sales tax was imposed, meets the test of being directly related to the educational and charitable purposes of the taxpayer.

The taxed sources of revenue include income from refreshment stands, product sales in the general store, hotel revenues, product sales outside the general store but within the village and the penny machine. While handmade dolls, candles, vending machine revenues and other sales taxed by the department are appropriate to the taxpayer's setting, their sale does not further the educational not-for-profit purpose of the taxpayer. These activities are not substantially related to the taxpayer's educational purpose. Therefore, these protested sales are most like the taxable sales of greeting cards by a church bookstore listed in example 5. Except for the sales of pony feed, the taxpayer's sales upon which sales tax was imposed do not directly further the taxpayer's educational and charitable purposes.

FINDING

The taxpayer's protest is sustained as to the imposition of sales tax on the vending machine sales of pony food. The remainder of the taxpayer's protests to the imposition of sales tax is denied.

II. Sales and Use Tax-Capital Assets

DISCUSSION

During the tax period, the taxpayer had several structures constructed. No sales tax was paid on the materials used in these building projects. The audit assessed use tax on the materials used in the construction of these capital assets. The taxpayer protested the assessments on the materials used in the construction of the Chautauqua Pavilion, the fixtures in the Chatauqua Pavilion and the materials used in building a Comfort Station on the basis that these capital assets further the taxpayer's exempt purpose.

Indiana imposes an excise tax on tangible personal property stored, used, or consumed in Indiana unless the sales tax is paid on the transaction. IC 6-2.5-3-2 (a).

The application of the use tax as it pertains to materials used in construction projects is clarified at 45 IAC 2.2-3-8 as follows:

- (a) In general, all sales of tangible personal property are taxable, and all sales of real property are not taxable. The conversion of tangible personal property into realty does not relieve the taxpayer from a liability for any owing and unpaid state gross retail tax or use tax with respect to such tangible personal property.
- (b) All construction material purchased by a contractor is taxable either at the time of purchase or if purchased exempt (or otherwise acquired exempt) upon disposition unless the ultimate recipient could have purchased it exempt.

Exemption from the use tax is granted to property used by qualified not-for-profit organizations under certain conditions at IC 6-2.5-5-25 (a) as follows:

Transactions involving tangible personal property or service are exempt from the state gross retail tax, if the person acquiring the property or service:

(a) is an organization which is granted a gross income tax exemption under IC 6-2.1-3-20, IC 6-2.1-3-21, or IC 6-2.1-3-22;

(2) primarily used the property or service to carry on or to raise money to carry on the not-for-profit purpose for which it receives the gross income tax exemption; and

(3) is not an organization operated predominantly for social purposes.

Sales Tax Division Information Bulletin #10 Revised February 10, 1986 deals with the exemption of not-for-profit corporation purchases for its own use from the use tax as follows:

1. In order to qualify for sales tax exemption on purchases as a not-for-profit organization the following conditions must prevail:

(a) The organization must be named or described in IC 6-2.1-3-19, 6-2.1-3-20, 6-2.1-3-21 or 6-2.1-3-22. This includes not-for-profit organizations organized and operated exclusively for one or more of the following purposes. . . Educational

(c) The organization is not operated predominantly for social purposes.

(d) In order for a purchase by a not-for-profit organization to qualify for exemption, the article purchased must be used for the same purpose as that for which the organization is being exempted. Purchases for the private benefit of any member of the organization or for any other individual, such as meals or lodgings, are not eligible for exemption. Purchases used for social purposes are never exempt.

The Pavilion and Comfort Station were both built in the village area of the taxpayer's operations. The Pavilion is covered with a cement floor that can be enclosed in inclement weather. The Comfort Station is a restroom facility in the village. These two facilities clearly meet the first three cited requirements to qualify for exemption. The issue is whether or not they meet the fourth requirement, that they are used for the "same purpose as that for which the organization is being exempted." School and other groups use it as a gathering and meeting place while in the village to further their understanding of a turn of the century village. The Comfort Station is also utilized by persons engaged in educational activities in the village. The use of these facilities and their fixtures further the exempt purpose, education, of the taxpayer. Therefore, the tangible personal property used in the construction of the Pavilion and the Comfort Station is exempt from the use tax.

FINDING

The taxpayer's protest to the assessments of use tax on materials used in the construction of the Pavilion, its fixtures, and the Comfort Station is sustained.

III. Sales and Use Tax-Supplies

DISCUSSION

Indiana imposes an excise tax on tangible personal property stored, used, or consumed in Indiana unless the sales tax is paid on the transaction. IC 6-2.5-3-2 (a). Exemption from the use tax is granted to property used by qualified not-for-profit organizations under certain conditions at IC 6-2.5-5-25 (a) and Sales Tax Division Information Bulletin #10 Revised February 10, 1986 as cited in the discussion of the taxpayer's use tax liability on materials used in the construction of capital assets.

During the audit period, the taxpayer did not pay sales tax when it purchased supplies for the operation of the village, farmstead and inn. The department assessed use tax on the use of these supplies and the taxpayer protested this assessment.. The taxpayer divided its protest into four categories: 100% village use; 100% use for production of membership mailings, promotions and related activities; proportionate uses for the inn and the village; and 100% inn use. The taxpayer meets the first three criteria for exemption. The issue to be determined is whether the taxpayer's purchase of supplies in the various categories further the taxpayer's educational purpose.

The supplies used 100 % in the village and for membership needs include such items as repair of village buildings, rock for village roadways, an antique carousel, trash bags, admission wrist bands, and bunting for decorations. The use of these items helps to maintain the village and add to the historical and educational experience. The supplies used in the membership area add to the member's utilization of the village and educational experiences there. Supplies purchased for use in these categories are exempt from the use tax.

The inn is a related proprietary business that doesn't further the exempt educational experience of the visitors. As such, supplies used at the inn are subject to the imposition of the use tax.

The last category, supplies that were purchased in bulk and a portion used in the village and a portion used in the inn are subject to the use tax to the extent they were used in the inn for the non-exempt purpose.

FINDING

The taxpayer's protest to the imposition of use tax on supplies is sustained to the extent the supplies were used in the village or for membership purposes. The taxpayer's protest to the imposition of use tax on supplies used in the inn is denied.

IV. Tax Administration-Penalty

DISCUSSION

The taxpayer's final protest concerns the imposition of the ten percent (10%) negligence penalty pursuant to IC 6-8.1-10-2.1. Negligence is defined at 45 IAC 15-11-2(b) as "the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer." Negligence is to "be determined on a case-by-case basis according to the facts and circumstances of each taxpayer." Id.

IC 6-8.1-10-2.1(d) allows the department to waive the penalty upon a showing that the failure to pay the deficiency was based on "reasonable cause and not due to willful neglect." Departmental regulation 45 IAC 15-11-2 (c) requires that in order to establish "reasonable cause," the taxpayer must demonstrate that it "exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed. . . ." The taxpayer presented substantial evidence showing that it met this burden. The negligence penalty does not apply in this situation.

FINDING

The taxpayer's protest is sustained.